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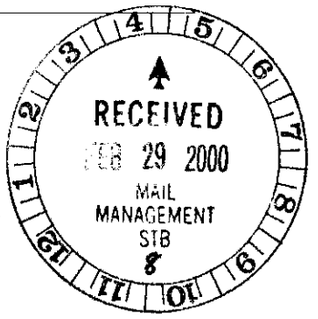
AMERICAN SHORT LINE AND
REGIONAL RAILROAD ASSOCIATION
The Voice of America's Independent Railroads

Alice C. Saylor
Vice President & General Counsel



February 29, 2000
Via Hand Delivery

Surface Transportation Board
Office of the Secretary, Case Control Unit
1925 K. Street, N.W.
Washington, D.C. 20423

ATTN: Ex Parte No. 582

Re: STB Ex Parte No. 582, Public Views on Major Rail Consolidations

Dear Sir:

Attached for filing with the Surface Transportation Board are the original and ten paper copies of the Statement of Frank K. Turner, President of the American Short Line and Regional Railroad Association in the above-captioned proceeding. A copy on diskette is also enclosed.

Please date-stamp the duplicate copy to indicate receipt and return it to the messenger. Thank you.

Sincerely,

Alice C. Saylor

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Before the
Surface Transportation Board
Washington, D.C.

STB Ex Parte No. 582, Public Views on Major Rail Consolidations

STATEMENT OF FRANK K. TURNER, PRESIDENT
AMERICAN SHORT LINE AND REGIONAL RAILROAD ASSOCIATION

Chairman Morgan, Vice Chairman Burkes, and Commissioner Clyburn, I am Frank Turner, President of the American Short Line and Regional Railroad Association ("ASLRRA"). In a Decision served January 24, 2000, the Surface Transportation Board ("Board") announced this public hearing to allow interested parties to express their views on the subject of major railroad consolidations, and the present and future shape of the North American railroad industry. ASLRRA and its 425 short line and regional railroad members have a critical interest in these subjects. We appreciate the opportunity for our views to be heard.

ASLRRA is a non-profit trade association that represents the interests of its more than 425 short line and regional railroad members in legislative and regulatory matters and industry affairs. ASLRRA was formed by the consolidation of the American Short Line Railroad Association with Regional Railroads of America effective January 1, 1998. Short line and regional railroads are an important and growing component of the railroad industry. Today, they operate and maintain 29 percent of the American railroad industry's route mileage, and account for 9 percent of the rail industry's freight revenue and 11 percent of railroad employment. Small railroads provide a vital link to shippers in many rural areas and play an essential role in the movement of many industrial and agricultural goods and commodities.

Short line and regional railroads, and the shippers and communities that depend on them for service, are deeply affected by the ongoing restructuring of the North American railroad industry. This extends to both the Class II and the Class III railroads, and I include both groups within the scope of my remarks.

The rail industry has been thoroughly transformed by the continuing series of Class I railroad mergers and the sale of hundreds of light density branch lines to new operators. This happened through incremental steps over the last twenty years which, taken together, have wrought remarkable changes. In the rail industry, the big have gotten much bigger, while the small have grown greatly in number. These changes have led to increased efficiencies, but this progress has come at a price.

As a group today, the small railroads are suffering from what I refer to as "merger fatigue." We have had to cope with continuous change in recent years as merger after merger has been implemented. The promised benefits and efficiencies have often been slow in coming or nonexistent, at least from our vantage point. Service failures have alienated some of our loyal shippers and wreaked havoc with our bottom lines. Personnel cuts that seem inevitably to come as the Class I's cut costs after a merger have put small railroads farther and farther away from Class I operating and marketing officials that they need to deal with on a day-to-day basis. Those Class I officials often seem stretched thin as they struggle to cope with expanded responsibilities.

These problems have led the Association to take a very serious and, frankly, rather skeptical look at whether further consolidations would be good or bad for the railroad industry and what the timing should be. In the past ASLRRA has remained neutral with regard to any particular Class I merger or acquisition transaction, because any particular transaction affects ASLRRA members differently depending on their situation. That has made it difficult for the Association to take an affirmative position, either pro or con. The small railroads as a group have basically left it to the Class I's and the Board to sort out their deals.

Today, however, many ASLRRA member railroads are deeply troubled by the prospect of another Class I merger. They have been badly hurt by past transactions, both by service problems related to implementation, and by post-transaction reduction in competitive options.

I am here today to articulate a set of conditions to protect the interests of small railroads while these Class I transactions take place. I agree with the Board's concern that the restructuring and realignment of the Class I's may not be over yet. Simply put, times have changed, and new rules are needed. With these protections which I will outline either voluntarily agreed to by the Class I parties or imposed by the Board as part of the merger approval process, the Association should be able to maintain its neutral stance, at least for the foreseeable future. If we cannot obtain these protections it is likely the Association will have to oppose future mergers.[1]

These new rules I am suggesting can be imposed by the Board as conditions in the context of its authority over future rail merger and consolidation transactions. They may also be appropriate for application to future negative impacts of recent merger and consolidation transactions that are still subject to Board oversight. These conditions are quite straightforward, few in number, easily understood, and utterly essential to protect the continued viability of small railroads as part of the interconnected rail network.

Together, they comprise what can be called a Short Line and Regional Railroad "Bill of Rights." I believe that these conditions should become an integral part of every Class I transaction approval process at the Board, present and future. Some or all of them may also be appropriate for application to recent transactions still subject to Board oversight. An expeditious enforcement/remedy process at the Board should be put in place to resolve disputes. The small railroads need this, and our national rail network deserves no less. These conditions will allow small railroads to remain viable competitors and feed traffic to the national system, whatever the future shape of the

[1] Looking down the road, I do not know what the Association's posture will be if we get to the point that there will just be two Class I rail systems left in North America. Although some have speculated that is where we are headed, I am not sure that is a good idea. It seems to me that the limited competitive options would be an invitation to reregulation, and I do not believe that would be in the best interests of the railroad industry.

North American rail network turns out to be. This is important to the system as a whole. Today, small railroads originate more than a fifth of the carloads moved by the Class I's.

Many of these conditions involve topics that are part of the Railroad Industry Agreement. This Agreement was signed in September of 1998. It resulted from private industry negotiations between representatives of the large and small railroads. The Agreement is limited in its application. Many of its most valuable commercial and competitive provisions apply only to traffic new to rail, and not to existing traffic. That was as far as the negotiations were able to go in 1998. However, despite some shortcomings, the Railroad Industry Agreement does provide a framework within which large and small railroads can deal with the some of their contentious issues.

So far, I would have to say that the results of the Agreement can best be described as very limited. It was certainly a positive thing for the industry to be able to successfully conclude such a negotiation and reach agreement outside of the regulatory process. However, I wish there were more clear successes under the Agreement to report to you today. Although the Agreement and what it stands for seem to be embraced at the Class I CEO level, it often seems to lose something in the translation on the way down to the troops that actually implement it.

I have recently suggested to the CEO's of all the major Class I railroads that we need to appoint representatives to sit down and initiate the next round of negotiations to try to strengthen the Railroad Industry Agreement. So far no talks have been scheduled. I hope this process can move forward. I urge the Board to repeat the approach that was so effective two years ago in Ex Parte No. 575: Require all the Class I's to sit down with small railroad representatives, with a tight time frame, to negotiate mutually agreeable solutions to the issues raised in this Statement and to report back to the Board by a specified date. These issues are: **Service, Interchange and Routing, Pricing, and Car Supply**. The Railroad Industry Agreement is a good

idea, but it needs to be taken further and given more teeth. This framework should become the standard governing our future relationships with the large carriers.

The items included in the Short Line and Regional Railroad "Bill of Rights" would provide an excellent starting point for this next round of industry-wide negotiations. I envision that we can fight on two fronts, or proceed on two parallel tracks if you prefer that metaphor. First, the Board can toughen the conditions required as part of the merger approval process for major transactions, with an expedited, complaint driven remedy process at the Board to enforce these conditions if necessary. At the same time, the industry can voluntarily discuss broadening the Railroad Industry Agreement to give the same principles a wider application outside the merger approval context. The result, I believe, will be a healthier and more competitive railroad industry.

THE SHORT LINE AND REGIONAL RAILROAD "BILL OF RIGHTS"

1. Small Railroads Have the Right to Compensation for Service Failures

Service disruptions have become routine following major Class I transactions, and time after time small railroads have suffered. The record is dismal. In each of the last several mergers, many small railroads experienced severe revenue erosion due to the inability of their Class I connection to handle normal business levels. Shippers turn to trucks. Once they do, some of them never come back even after service improves.

Some service problems are clearly related to traffic growth, capacity constraints and inadequate infrastructure within the railroad industry. These problems are real, and underscore the critical need for major continuing capital investment by the railroad industry. Unfortunately, however, the service problems are also related to ineffective planning and poor execution of merger transactions. Time and again, claimed benefits have not materialized, while problems that were not supposed to occur have.

The difficulties small railroads face when service disruptions occur is often made worse by unavailability of Class I operating personnel. Personnel cuts in the name of efficiency seem inevitably to follow merger approval. The local Class I trainmaster is the first point of contact on operating issues for a small railroad. After a merger, the trainmaster typically ends up with a much larger territory to cover and is often located farther away. It is tough to address and resolve local problems under these conditions.

Before a merger takes place, connecting small railroads should be involved in the Class I's planning for implementation. The Class I's should be required to brief all connecting short lines and regionals. This dialogue at the local level could help avoid some of the service problems that have plagued recent mergers.

After a transaction is implemented, small railroads can be part of the solution if service problems occur. Indeed we have played that role in past mergers by rerouting trains, doing extra switching and blocking, etc. for our Class I partners. We are glad to do what we can to help. However, this should not include suffering revenue losses due to merger-related service failures over which we have no control.

From now on, **no Class I merger or acquisition transaction should be approved without iron-clad guarantees that short line and regional railroads will receive prompt compensating payment from the Class I to make up for revenue losses directly caused by service or local operating deficiencies resulting from the transaction. When a Class I cannot provide an acceptable level of service post-transaction, small railroads should be allowed to perform additional services as necessary to provide acceptable service to shippers.**

Shippers already have some rights to compensation when serious service problems occur. Small railroads should be provided a right to compensation, too. This can be put in place by agreement of the merging Class I parties if the Board makes it a condition of its merger approval.

2. Short Line and Regional Railroads Have a Right to Interchange and Routing Freedom

The competitive landscape has been radically altered as a result of the continuing series of Class I mergers and acquisitions. Many viable alternative routes have been eliminated, either by physical removal or economic disadvantage. This has hampered the small railroads' efforts to hold onto existing business or attract new business to rail. This often creates "captive railroads."

Connectivity within the railroad industry has not been treated as a priority. Today's railroad industry, driven by Class I railroad policies and actions post-Staggers, has minimized rather than maximized rail routing options. These actions and policies may have yielded some short-term benefit to the Class I's for a while, although shippers and short lines have complained and protested but largely to no avail. Now, however, the industry is paying the price. The cumulative effect of the widespread elimination of routes through gateway closings, pricing policies, "de-marketing" of some business, and restrictions in line sale agreements through the 1980's and 90's have added up to the point that today there is often literally nowhere to go when rail lines become clogged.

I believe that the rail system must be truly interactive to function at peak efficiency. At junctions and terminal areas, small railroads should have the right to interchange with all Class I carriers as well as with each other without being disadvantaged in any way in terms of operations or pricing. Artificial "paper barriers" which arbitrarily restrict full interchange rights should be eliminated. Gateways, through routes and joint rates should be preserved as long as they are reasonably efficient, or allowed to be re-established if previously eliminated.

Up until now the Board and the ICC before it have chosen not to interfere with barriers to competition in line sales agreements. This may have been appropriate in the

past when the primary goal was to encourage line sales as an alternative to abandonment. However, today the industry has changed so much that the focus should be more on fostering competition among the railroads as the number of Class I's continues to decline.

Some have argued that "paper barriers" were agreed to by the buyers as part of a negotiated contractual line sale agreement, and formed part of the basis for the sale price. That argument was valid. However, circumstances have changed substantially since the mid-1980's and early 1990's when many of these line sales took place. First of all, considerable time has passed. The selling Class I has enjoyed the benefit of its bargain - - restricted competitive options for the spun-off line - - for quite a few years. Also, the world is very different. In essence, the deal has changed with the radically changing times. There are far fewer Class I railroads today. That has changed the competitive landscape to the point that artificial restrictions are no longer tolerable.

From now on, **no Class I merger or consolidation transaction should be approved without a requirement that all contractual barriers that prohibit or disadvantage full interchange rights, competitive routes and/or rates must be immediately removed, and none imposed in the future. Also, small railroads should be free to interchange with all other carriers in a terminal area without pricing or operational disadvantage.**

3. Short Line and Regional Railroads Have a Right to Competitive and Nondiscriminatory Pricing

This subject has several aspects. Class I carriers would be prohibited from practices which discriminate between their (Class I) customers and those located on connecting short lines. Pricing should be market based. Real capital and operating cost differences are valid, but Class I pricing should not disadvantage a customer

located on a small railroad for that reason alone. Small railroads must be able to quote competitive rates for their shippers, and must not be artificially prevented from doing so.

The prohibition against discriminatory pricing which disadvantages a customer located on a small railroad has particular application in the case of some western grain rates. Rates for movement of grain can, and do, reflect efficiencies in train loading and movement. A series of discounts are often made available off the transportation rate for movement in unit trains or multi-car lots, rapid loading capability, etc. These discounts are proper and pro-competitive when they reflect actual savings and operating efficiencies to the Class I railroad. For instance, it is operationally simpler and there are savings in terms of locomotives, crews, fuel, time and track capacity usage when a Class I railroad picks up an assembled unit train of grain to haul, compared to when it must perform multiple switches in order to assemble the train. It is one thing for the discounts to reflect actual savings and efficiencies. In my view, that is pro-competitive and proper. However, when the discounts are denied to a unit train assembled from multiple loading points on a small railroad, where the small railroad is willing to absorb the extra switching required to assemble the unit train, and that unit train is identical to the unit train loaded at a Class I loading point that gets the discounts, that is something else again. I call that discrimination, and I believe it is an anti-competitive practice.

After a merger or consolidation, the merging carriers should be required to quote through rates in conjunction with connecting railroads; or, alternatively, proportional rates on the Class I segment of a route that will enable the small railroad to quote a competitive rate for the entire movement. This will enhance competitive options.

The Board should expressly prohibit discrimination against customers located on small railroads as a condition of any Class I transaction, and provide a user-friendly remedy at the Board for small railroads with complaints.

From now on, **no Class I merger or acquisition transaction should be approved without an express requirement that rates and pricing for small railroads will be competitive and nondiscriminatory.**

4. Short Line and Regional Railroads Have a Right to Fair and Nondiscriminatory Car Supply

An adequate and suitable car supply is a fundamental requirement to do business as a railroad. Small railroads cannot succeed without fair access to needed equipment from their Class I partners.

Much of the freight originated or terminated on a small railroad spends the majority of its journey on a Class I railroads. The Class I typically receives a proportionately larger share of the freight revenue as well. Many small railroads own or lease a substantial amount of rail equipment to serve the needs of their shippers and protect their loadings. However, they must depend on their Class I connection(s) to do their share in supplying cars as well. This has always been true historically, and it remains the case today.

The movement of joint line freight requires cooperation between the rail partners. This includes cooperation in obtaining and supplying suitable equipment. This obligation extends to a willingness to agree to pay fair amounts of car hire, and a commitment to make equipment available for loading equitably, even in times of shortage. When equipment shortages occur, available cars should be furnished on a proportional basis among the Class I and short line shippers. The Class I should be liable for the small railroad's lost earnings when this standard is not met.

From now on, **no Class I merger or consolidation transaction should be approved without a requirement that connecting small railroads will be treated in**

a fair and nondiscriminatory fashion with regard to car supply and car compensation.

* * * * * * *

The railroad industry is in a period of continuing structural change. The resulting changed relationships and service disruptions have a serious impact on small railroads. Small railroads are an essential and valuable part of the national network. These small businesses need some fundamental assurances if they are to remain viable in the future.

I urge the Board to require these assurances from the Class I railroads involved in all major transactions that come before the Board for approval from this day forward. They could also be considered as a remedy for future negative impact from Class I mergers that are still open for Board oversight. **The right to compensation for service failures - - The right to interchange and routing freedom - - The right to competitive and nondiscriminatory pricing - - The right to fair and nondiscriminatory car supply** - - These are the bare minimum required to give small railroads a fair chance to survive in the brave new world of Class I railroading. An expedited complaint driven remedy procedure at the Board should be available to sort out problems with implementation of these conditions.

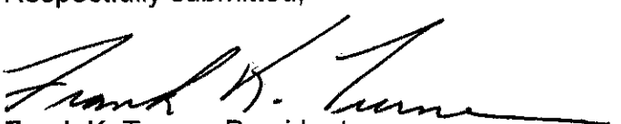
These concepts all grow out of the Board's charge under the National Rail Transportation Policy to "ensure the development and continuation of a sound rail transportation system with effective competition among rail carriers... To foster sound economic conditions in transportation and to ensure effective competition and coordination between rail carriers and other modes." The National Rail Transportation Policy envisions allowing competition to be the regulator wherever possible, and to minimize the need for Federal regulatory control. However, competition has become

less effective in protecting small railroad interests as access to competing Class I railroads has been reduced.

I will commit, on behalf of the short line and regional railroads, to make every effort to move forward with another round of negotiations to deal with as many of these issues as possible in the context of the Railroad Industry Agreement and report back to the Board promptly. It would certainly help if the Board would give its encouragement to this process and set some firm deadlines. At the same time, I urge the Board to adopt the points of the "Short Line and Regional Railroad Bill of Rights" as a minimum requirement for conditions to be accepted as part of any Class I merger or consolidation transaction from this day forward.

Thank you.

Respectfully submitted,



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Date: March 8, 2000